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No. 88-94

In the Supreme Court of the United States

October Term, 1988

KENTUCKY WEST VIRGINIA GAS COMPANY
and
EQUITABLE GAS COMPANY, A DIVISION OF
EQUITABLE RESOURCES, INC.,
Petitioners

v.

PENNSYLVANIA PUBLIC UTILITY COMMISSION
and
PENNSYLVANIA OFFICE OF CONSUMER ADVOCATE,
et al.,
Respondents

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE THIRD CIRCUIT

BRIEF OF RESPONDENT, PENNSYLVANIA PUBLIC UTILITY COMMISSION IN OPPOSITION

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QUESTIONS PRESENTED

1. Whether the United States Court of Appeals for the Third Circuit committed error in upholding a state agency's disallowance of certain wholesale gas costs claimed by a utility when no showing was made before the agency or the District Court that the costs were unavoidable and entitled to recovery under the "filed rate" doctrine?

2. Whether Pennsylvania's least cost fuel procurement policy embodied in Act 74 constitutes a new cost recovery standard that achieved a taking of utility property in violation of the Fifth Amendment and the Due Process Clause of the Fourteenth Amendment?

3. Whether an order of a state agency directing a publicly regulated utility to employ counsel independent of its affiliated supplier violated that utility's right to counsel or its freedom of speech?

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BRIEF OF RESPONDENT PENNSYLVANIA PUBLIC UTILITY COMMISSION IN OPPOSITION

Respondent Pennsylvania Public Utility Commission ("PaPUC"), an independent administrative commission authorized to exercise plenary authority over the rates and services of public utilities in the Commonwealth of Pennsylvania pursuant to the provisions of the Public Utility Code, Title 66 Pennsylvania Consolidated Statutes Anno-

tated §§101 *et seq.*, submits this Brief In Opposition To The Petition For A Writ Of Certiorari To The United States Court Of Appeals For The Third Circuit at No. 87-5052.

COUNTER-STATEMENT OF THE CASE

The PaPUC concurs in the majority of factual assertions made by Petitioners Kentucky West Virginia Gas Company and Equitable Gas Company, a division of Equitable Resources, Inc. ("Petitioners" or "Kentucky West").[1] Petitioners are incorrect, however, when they argue in their Statement that the PaPUC took action against Equitable that was similar to state action barred by this Court's recent decision in *Mississippi Power & Light Co. v. Mississippi*, U.S. , 108 S.Ct. 2428 (1988). Equitable suggests that while before the PaPUC it defended its gas purchases from its affiliated supplier, Kentucky West Virginia Gas Company, as being consistent with Act 74's requirements due to the existence of a minimum bill obligation with that pipeline supplier. Petition at 6-7. In fact, Equitable's primary defense of Kentucky West purchases was based on its belief that a pro rata purchasing strategy dictated a certain level of purchases from Kentucky West so that a reliable supply of gas would be available from that Company in the future. App., *infra*, 116a, 124a.

Equitable's Statement also makes other important omissions that bear on the issue of whether the PaPUC ignored minimum bill costs. Due to demand constraints in 1983 and 1984 Equitable invoked the *force majeure* clauses in its gas contracts with Tennessee Gas Pipeline

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[1] Occasional references will be made to "Equitable" to distinguish Equitable Gas Company, a distributor of gas, from its pipeline supplier, Kentucky West.

Company, Texas Eastern Transmission Corporation and Kentucky West Virginia Gas Company and declined to pay any minimum bill charges. It "informed its suppliers that Equitable would pay only for gas taken." App., *infra*, 128a. At the time the PaPUC decided Equitable's 1985 gas cost proceeding, the Company had not made any minimum bill payments to Kentucky West. App., *infra*, 128a, 132a. Equitable argued before the PaPUC that its costs incurred from Kentucky West should be granted a pass-through because this supply was more reliable than gas from Tennessee or Texas Eastern and that denial of any costs actually paid Kentucky West would constitute an attempt by the agency to redetermine FERC approved pipeline rates. App., *infra*, 117a, 124a.

Equitable's complaint filed with the District Court for the Middle District of Pennsylvania alleged that certain sections of Act 74 and the PaPUC order violated the Supremacy Clause of the U.S. Constitution. The complaint mentions the need to purchase gas below minimum bill levels but it did not allege that the PaPUC improperly refused to allow Equitable to collect unavoidable minimum bill costs from ratepayers. C.A. App. 9-25.[2] Rather, the complaint contended that the Natural Gas Act and the Natural Gas Policy Act guaranteed Equitable the right to pass-through to its customers any cost incurred pursuant to any FERC approved rate regardless of the availability of lower cost alternative supplies. C.A. App. 22. Specifically, Equitable asked the District Court to "declare costs in-

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[2] Equitable's complaint refers to a $713,000 disallowance of minimum bill costs by the PaPUC. C.A. App. 19. However, this statement refers to a disallowance relating to a prospective twelve month period ending July 31, 1986 that the PaPUC adopted due to Equitable's historic failure to pay minimum bill charges. This adjustment has not been challenged by Kentucky West.

curred or to be incurred by Equitable pursuant to any FERC approved tariff rate schedule to be just and reasonable as a matter of law for purposes of the Pennsylvania Public Utility Code". C.A. App. 24. Equitable's complaint was factually incorrect when it alleged that minimum bill contract provisions required it to "purchase" a minimum amount of gas. C.A. App. 16. The District Court found that a minimum bill, while typically requiring a payment, does not require the "purchase" of gas. App., *infra*, 45a.

Kentucky West's first attempt to show that the PaPUC had ignored unavoidable minimum bill charges materialized in its brief to the Court of Appeals through a calculation found in a footnote that was the subject of a Motion To Strike by the PaPUC. The Court of Appeals specifically found that the record did not support the inference that minimum bill costs had been blocked since Equitable never challenged before the District Court the PaPUC's findings that minimum bill payments had not been made to Kentucky West and that the prospect of future minimum bill payments was too speculative to justify their inclusion in rates. App., *infra*, 21a, 35a-36a.

Equitable fails to mention that its refusal to pay Kentucky West any minimum bill charges was resolved by a Federal Energy Regulatory Commission ("FERC") order issued after the PaPUC concluded its 1985 Act 74 investigation. *Kentucky West Virginia Gas Co.*, 33 FERC ¶ 61,240 (1985). Following this settlement with Kentucky West, Equitable requested recovery of $2.5 million in minimum bill costs paid to Kentucky West that related to the $14.3 million disallowed in the 1985 proceeding. The PaPUC allowed recovery of this claim in 1987 in consideration of the fact that it constituted minimum bill costs owed to Kentucky West and the payment of this minimum bill

was unascertainable in the 1985 proceeding. *PaPUC v. Equitable Gas Co.*, 87 PUR 4th 131, 138 (1987); C.A. App. 762-770.[3]

REASONS FOR DENYING THE PETITION

A. This Court Should Not Exercise Its Discretion To Review Whether the "Filed Rate" Doctrine Was Violated When There Was no Showing at Trial That Unavoidable Wholesale Costs Were Denied Recovery in Retail Rates

1. Kentucky West has not demonstrated that the PaPUC disallowed unavoidable minimum bill costs.

It is clear from Kentucky West's Petition for the Grant of Certiorari that it has discarded its attack on the facial constitutionality of Act 74 and its theory that a state agency must allow the pass-through of all costs incurred pursuant to any FERC approved rate. These claims were the heart of Kentucky West's complaint before the District Court. Kentucky West has now moved to center stage an argument not raised before the District Court to the effect that the PaPUC ignored minimum bill costs imposed on Equitable by Kentucky West and thus violated the "filed rate" doctrine. *Montana-Dakota Utilities Co. v. Northwestern Public Service Co.*, 341 U.S. 246 (1951); *Arkansas-Louisiana Gas Co. v. Hall*, 453 U.S. 571 (1981).

The Court of Appeals did not commit error when it declined to agree with Kentucky West regarding this mini-

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[3] Equitable Gas Company made an additional claim for $10.2 million in Kentucky West minimum bill costs relating to the 1983-1984 period in its recently concluded 1988 gas cost recovery proceeding before PaPUC. This claim was rejected because Equitable did not satisfy its burden of proof to demonstrate that these costs had actually been paid to Kentucky West. In addition, payment of such amounts conflicted with the settlement of minimum bill liability previously reached with Kentucky West. *PaPUC v. Equitable Gas Co.*, No. R-880932, Slip Op. at 5-13 (September 1, 1988).

mum bill argument. Kentucky West's failure to adequately raise and substantiate this issue below is well documented by the record. It is clear that at the time the PaPUC decided the 1985 gas cost recovery proceeding, Equitable had taken the position that it was legally excused from paying its pipeline supplier's minimum bills due to a declaration of *force majeure*. App., *infra*, 128a. Equitable's policy was to pay only for gas actually taken. *Id*. The basis of the PaPUC adjustment was that given this policy, Equitable did not purchase or take gas in a manner that would produce the lowest cost result for its retail customers. Kentucky West contends that the PaPUC ignored minimum bill liability since it failed to recognize "an FERC-imposed duty to purchase gas from Kentucky West and pay the tariff rate for that gas." Petition at 17. This statement is misleading since Equitable was never under any obligation to physically take gas from Kentucky West. The District Court recognized that a minimum commodity bill, while ordinarily requiring a payment, does not require the purchase of gas. App., *infra*, 45a.[4]

The District Court found that the PaPUC had not improperly disallowed any FERC approved rate. App., *infra*, 59a-60a. When Kentucky West presented the argument that the PaPUC had ignored unavoidable minimum bill

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[4] In footnotes 12 and 16 Petitioners attempt to designate the amounts paid to Kentucky West for gas actually taken in 1983 and 1984 as minimum bill costs. This characterization is apparently adopted to rationalize Equitable's failure to claim the entire, supposedly unavoidable, Kentucky West minimum bill before the PaPUC and to make the claim before the District Court for recovery of amounts paid to Kentucky West synonymous with a claim for "minimum bill" costs. Kentucky West, in footnote 16, erroneously refers to "federally required purchases" being at issue in this case. The Kentucky West tariff did not *require* any purchases. Moreover, minimum bill obligation does not attach to gas taken. When applied, it increases a buyer's costs for quantities of gas *not taken*.

costs before the Court of Appeals, the Court noted Kentucky West's failure to raise and substantiate this claim below:

> In conformity with our power of plenary review, we undertook a time-consuming analysis of the proceedings below to ascertain whether Equitable had raised the question of its minimum bill obligation in the context now developed on appeal. We conclude that Equitable failed to provide an analytic framework supporting an argument that the $14.3 million disallowance represented an unavoidable FERC-approved contractual obligation. *The record simply does not demonstrate that any portion of the disallowed costs represented Equitable's minimum bill obligation.*
>
> * * *
>
> The PUC found that no minimum bill costs had ever actually been incurred, and therefore declined to take them into consideration in setting the retail rate for the period in question. This uncertainty as to what minimum bill costs, if any, would *ever* be incurred by Equitable also justified the PUC's refusal to consider minimum bill liability in evaluating whether Equitable has pursued a least cost fuel procurement policy for the twelve month period under examination.
>
> * * *
>
> Finally, with respect to the challenge to the disallowance of allegedly unavoidable costs, *the only portion of the $14.3 million which could be characterized as unavoidable costs would be minimum bill charges actually incurred*. As we noted previously, the PUC disallowed the pass-through based on its findings that the purchases from Kentucky West were imprudent, even

> though already below minimum bill levels, because cheaper gas was available from alternate suppliers, *no minimum bill payments had ever been made to Kentucky West by Equitable*, and the likelihood that such payments would ever be made was too speculative and uncertain to justify inclusion of them in Equitable's estimated cost of service. Those findings were unchallenged before the district court, and the first finding above was affirmed by the Pennsylvania Commonwealth Court. Therefore, *this record cannot support an inference that the costs were unavoidable*.

App., *infra*, 21a, 35a-36a. (Emphasis added.) The appropriateness of the finding below regarding minimum bill is further bolstered by the fact that in 1987, the PaPUC allowed Equitable to collect the minimum bill expense that related to the $14.3 million adjustment after FERC approved a Kentucky West/Equitable settlement of the minimum bill controversy. FERC modified Kentucky West's minimum bill by approving a settlement agreement. *Kentucky West Virginia Gas Co.*, 33 FERC ¶ 61,240 (1985). Equitable was granted recovery of $2.5 million in Kentucky West minimum bill charges by the PaPUC in *PaPUC v. Equitable Gas Co.*, 87 PUR 4th 131 (1987):

> Equitable now contends that the adjustment approved at Docket No. R-850038 is incomplete in that it failed to reflect the minimum bill effect of disallowed Kentucky West purchases.
>
> * * *
>
> In this proceeding the Company has adjusted its purchased gas costs by $2,552,833 which represents only the fixed cost portion of its alleged $15,000,000 minimum bill deficiency to Kentucky West under the Commission's previously approved gas supply mix.
>
> * * *

> Therefore we will permit Equitable to include in rates that fixed cost portion of those gas volumes below minimum bill. This is consistent with our understanding of the operation of FERC approved minimum bills.

C. A. App. 766, 772.

Before this Court can reach the issue of whether a denial of a utility's minimum bill liability by a state agency conflicts with the "filed rate" doctrine it must overturn the fact finding performed by the PaPUC and District Court and find that the Court of Appeals erred in ruling on whether the minimum bill issue had been properly raised. This is a prerequisite because the underlying assumption of Kentucky West that an unavoidable FERC approved cost was ignored has not been established below or even properly raised in the view of the Court of Appeals. A grant of certiorari would place this Court in the position of addressing an issue of alleged conflict with the "filed rate" doctrine that was not dealt with, for good reason, by the Court of Appeals. This Court has observed that certiorari is not granted to review evidence and discuss specific facts. *United States v. Johnston*, 268 U.S. 220, 227 (1985). A fact crucial to Kentucky West's argument—that the PaPUC refused to pass-through in retail rates an unavoidable FERC approved cost incurred by Equitable—has not been established below.

Neither the District Court nor the Court of Appeals found facts that support Kentucky West's theory that the PaPUC "trapped" FERC approved costs by refusing to pass-through unavoidable minimum bill costs. To the contrary, the Court of Appeals found that no factual support existed for Kentucky West's allegation that the PaPUC set rates that "trapped" FERC approved costs. The fact finding

of the PaPUC that established the failure of Equitable to incur and pay minimum bill expenses should be given the same preclusive effect as the fact finding of state courts. *University of Tennessee v. Elliot*, 478 U.S. 788 (1986).

The Courts below have determined that the record does not support a finding that the PaPUC denied recovery of an unavoidable FERC approved expense. Kentucky West has simply not provided this Court with a factual foundation that allows the Court to explore the legal issue it raises of conflict between state ratemaking authority and the "filed rate" doctrine. Moreover, Kentucky West has not explained why a grant of certiorari is appropriate given Equitable's request and receipt of minimum bill costs relating to the $14.3 million adjustment in its 1987 rate proceeding. This Court should leave the findings of the Courts below undisturbed and decline to grant review.

2. Current FERC policy renders the issue of conflict between state ratemaking treatment of pipeline minimum bills and the "filed rate" doctrine unimportant and not worthy of review.

Kentucky West has not established that the PaPUC ignored unavoidable minimum bill expenses in setting intrastate retail rates for Equitable.[5] Even if the facts were as Kentucky West alleges, the need for the Court to reach this issue is diminished by the fact that FERC has moved to eliminate this type of tariff provision from the tariffs of interstate pipelines. Guidance from the Court on this issue is simply not warranted given the passing of minimum bills from the scene of interstate pipeline tariffs.

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[5] Kentucky West suggests that FERC agrees with its analysis that the PaPUC was "obligated to take account" of FERC-approved tariffs. FERC however, has never joined Kentucky West in its argument that the PaPUC ignored unavoidable FERC approved charges in its rate order and has not taken a position on the factual basis for Equitable's claim.

Pipeline minimum commodity bills were generically attacked by FERC in 1984 when it directed the removal of variable costs from pipeline minimum commodity bills. *Elimination of Variable Costs From Certain Pipeline Minimum Commodity Bill Provisions*, 27 FERC ¶ 61,318 (1984). At that time FERC allowed fixed-costs to remain in pipeline minimum bill tariff provisions. However, in subsequent proceedings involving individual pipelines, FERC has resolutely moved to eliminate the minimum bills altogether.

At the time of the PaPUC order at issue in this case, Equitable was served by three interstate natural gas pipelines-Kentucky West Virginia Gas Company, Tennessee Gas Pipeline Company and Texas Eastern Transmission Company. In an order issued on June 22, 1988, the FERC eliminated Kentucky West's minimum commodity bill retroactive to March 2, 1986 having found the bill to be "anticompetitive". *Kentucky West Virginia Gas Company*, 43 FERC ¶ 61,496 (1988).[6] FERC has also struck down the minimum bills of Equitable's two other pipeline suppliers. *Tennessee Gas Pipeline Company*, 36 FERC ¶ 61,071 (1986): (The minimum bill is anticompetitive and produces an inequitable result); *Texas Eastern Transmission Corporation*, 43 FERC ¶ 61,076 (1988): ("Texas Eastern does not need minimum bills to compete . . . .").

The elimination of minimum bills by FERC is not a phenomenon that has only involved Equitable's pipeline suppliers. It has affected the natural gas industry nationwide. *ANR Pipeline Co.*, 37 FERC ¶ 61,263 (1986): ("[O]ur review of the initial decision and the record demonstrates that ANR's minimum bills are unlawful and should be

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[6] This order is currently the subject of a Request for Rehearing at FERC.

eliminated."); *Panhandle Eastern Pipe Line Co.*, 38 FERC ¶ 61,164 (1987): (FERC affirms ALJ finding that the minimum bill is anticompetitive and should be eliminated from the LS and SS schedules); *Transcontinental Gas Pipe Line Corporation*, 44 FERC ¶ 61,216 (1988): ("Transco must eliminate its minimum bill effective April 1, 1987."); *Transwestern Pipeline Co.*, 32 FERC ¶ 61,009 (1985) *affirmed Transwestern Pipeline Co. v. FERC*, 820 F.2d 733 (5th Cir. 1987): ("[W]e affirm the judge and hold that Transwestern's minimum bills are unduly discriminatory and therefore unlawful . . . .").

Kentucky West has argued to this Court that it should grant certiorari so that "confusion" will not be created in the future by the Court of Appeals decision. However, FERC's steady elimination of pipeline minimum bills makes it unlikely that future litigation will arise on the issue of conflicts between state agency treatment of minimum bills and the "filed rate" doctrine. Obviously, the issue will not be of continuing importance to Equitable as all three of its pipeline suppliers have lost their minimum bills. The question raised by Kentucky West of whether the Court of Appeals failed to recognize a conflict between state ratemaking involving minimum bills and the "filed rate" doctrine is not relevant to potential future controversies. No useful guidance to future parties and the Courts would be gained by granting review of this issue.

B. The Decision of the Court of Appeals Fully Comports With *Nantahala* and *Mississippi Power*

Kentucky West attempts to show that conflict exists between the decision of the Court of Appeals and this Court's recent decisions involving the "filed rate" doctrine in *Nantahala Power & Light Co. v. Thornburgh*, 476 U.S.

953 (1986), and *Mississippi Power & Light Co. v. Mississippi*, U.S. , 108 S.Ct. 2428 (1988). Neither of these cases bars the action of the PaPUC taken with respect to Equitable's retail rates. Together, *Nantahala* and *Mississippi Power* provide a recent, clear explanation of the limits of state ratemaking vis-a-vis the "filed rate" doctrine by this Court such that no further elaboration of the boundaries of state and federal ratemaking authority is necessary.

Nantahala clearly set forth the proposition that state agencies may not alter FERC approved rates for retail rate purposes such that costs are "trapped" between the actual wholesale FERC rate paid and the retail rate permitted. This Court, however, specifically separated from its holding in *Nantahala* the situation where a utility has an array of wholesale energy rates available to it, including FERC approved rates, and does not select the supplier that will produce the lowest retail rate:

> Without deciding this issue, we may assume that a particular quantity of power procured by a utility from a particular source could be deemed unreasonably excessive if lower cost power is available elsewhere, even though the higher-cost power actually purchased is obtained at a FERC-approved, and therefore reasonable price.

476 U.S. at . This qualification to *Nantahala* was fully understood by the Court of Appeals which found it applicable to the present case:

> Although *Nantahala* underscores that a state cannot independently pass upon the reasonableness of a wholesale rate on file with FERC, it in no way undermines the long-standing notion that a state commission may legitimately inquire into whether the retailer prudently chose to pay the FERC-approved wholesale

> rate of one source, as opposed to the lower rate of another source.
>
> We interpret *Nantahala* as preempting state commissions from questioning or altering the wholesale rate and compelling them to accept it when determining pass-through in their retail rate-setting procedures.

App., *infra*, 17a. The Court of Appeals thus upheld the District Court's finding below that no conflict existed between the "filed rate" doctrine and the PaPUC order:

> The PUC did not disallow any FERC approved rate or any rate FERC must accept as a consequence of the NGPA. It accepted all of those rates as they appeared in Equitable's suppliers' cost structures. It simply chose from among all of those competitors, the gas supply that, in its view, would have resulted in the lowest cost to Equitable.

App., *infra*, 59a. The District Court had recognized the distinction previously made by the Pennsylvania Commonwealth Court in *Pike County Light and Power Co. v. PaPUC*, 77 Pa. Commonwealth Ct. 268, 465 A.2d 735 (1983) between a state agency's illegal review of the reasonableness of a FERC approved rate and an inquiry into the prudence of a utility's purchase decision given alternative supply sources. *Pike* at 274-5, 738. In 1985, the PaPUC engaged in a permissible review of Equitable's purchasing decision.

Although *Mississippi Power* was not available at the time the Court of Appeals rendered its decision, it requires no modification of the Court's result. This Court held in *Mississippi Power* that a state investigation of utility prudence was barred when FERC created an unavoidable obligation on the part of a utility customer to pay its

share of plant costs. *Mississippi Power* involved FERC's allocation of costs on a highly integrated affiliated utility system. FERC has not only set a wholesale rate, but it ordered the retail utility, Mississippi Power & Light, to pay for high-price Grand Gulf power. *Id.* at 2440. Again, as in *Nantahala* this Court noted, however, that:

> it might well be unreasonable for a utility to purchase unnecessary quantities of high cost power, even at FERC-approved rates, if it had the legal right to refuse to buy that power.

Mississippi Power at 2440.

Kentucky West failed to convince the District Court or the Court of Appeals that it was faced with an FERC-approved legal obligation to incur costs that implicated the "trapping" of costs prohibited by *Nantahala* and *Mississippi Power*. This failure on the part of Kentucky West to establish facts that bring its case within the bounds of *Nantahala* and *Mississippi Power* demonstrates that there is no conflict between the Court of Appeals' decision and the recent decisions of this Court involving the "filed rate" doctrine. The parameters of this doctrine are clear and require no further elaboration. No ambiguity remains after *Nantahala* and *Mississippi Power* that merits the grant of certiorari. *McDaniel v. Sanchez*, 452 U.S. 130, 136 (1981). The absence of conflict between the Court of Appeals and the recent decisions of this Court argues in favor of denying review.

C. Act 74 Did Not Create a New Ratemaking Standard That Effected a Confiscation of Equitable's Property

Kentucky West argues that Act 74 imposed a new ratemaking standard on utilities that could not have been anticipated by investors. Thus, according to Petitioners,

the PaPUC's rate disallowance effected a "taking" of property without due process in violation of the Fifth and Fourteenth Amendments. In response, PaPUC submits that Act 74 did not impose a new rate "standard" and that Kentucky West has failed to establish that any confiscation of property has occurred.

It is contended by Kentucky West that the PaPUC applied new and different standards to gas cost recovery claims when it commenced administering Act 74 after its effective date on July 30, 1984. Kentucky West alleges that the PaPUC moved from a standard of "just and reasonable" to the standard of least cost procurement. Act 74 did not repeal the basic mandate in Section 1301 of the Public Utility Code that "*[e]very* rate made, demanded, or received by any public utility, . . . shall be just and reasonable. . . ." (Emphasis added.) 66 Pa. C. S. 1301. Moreover, Act 74, did not modify the PaPUC's ongoing duty to only set rates that are "just and reasonable". The Act itself references the "[d]etermination of just and reasonable natural gas rates" and informs us that "[n]o rates for a natural gas distribution utility shall be deemed *just and reasonable* unless the commission finds that the utility is pursuing a least cost fuel procurement policy, consistent with the utility's obligation to provide safe, adequate and reliable service to its customers". (Emphasis added.) App., *infra*, 173a.

Kentucky West has failed to show that the era of the PaPUC's "just and reasonable" standard that supposedly expired when Act 74 became effective, in any way conflicted with Act 74's requirement that utilities follow a least cost fuel procurement policy. Although the Act requires the PaPUC to make a variety of specific fact findings regarding procurement activity of utilities that previously were discretionary, the basic mandate that utilities obtain

the lowest cost gas available was in effect before Act 74 became effective.

Prior to the passage of Act 74, the PaPUC set gas cost recovery rates according to the GCR (Gas Cost Recovery) procedure. This mechanism was first employed in 1978 and continued in effect until Act 74 was implemented. *Re Gas Cost Rates*, 52 PaPUC 217, 220 (1978): ("The Commission shall continuously review the reasonableness and lawfulness of the amounts of the charges produced by the gas cost rate and the charges included therein.") As with any fuel adjustment clause procedure, recovery of costs was dependent upon the utility making prudent, reasonable, low cost purchases of fuel. *Metropolitan Edison v. PaPUC*, 62 Pa. Commonwealth Ct. 460, 466-67, 437 A.2d 76, 80-81 (1981): (Metropolitan Edison failed to exercise proper managerial prudence in administering its coal contracts and as a result of imprudence, ratepayers were forced to pay unjust and unreasonable rates under the utility's fuel adjustment clause.)

The "least cost" procurement standard of Act 74 was essentially in effect as a ratemaking standard when utilities, including Equitable, were governed by the GCR process. The PaPUC stated in *Re Gas Cost Rate No. 5*, 58 PUR 4th 369 (1984):

> We will not hesitate to exercise our full authority to withdraw the authorization to utilize the *GCR* of any utility that continually ignores its obligations *to aggressively seek the lowest cost gas for its customers.*

58 PUR 4th at 374 (Emphasis added.) It is clear that the "least cost" objective was applied to Equitable and other gas utilities prior to the application of Act 74. Indeed it has always been a basic tenet of ratemaking jurisprudence that a utility is obligated to avoid excessive and unnecessary ex-

penditures. *Chicago & Grand Trunk Ry. Co. v. Wellman*, 143 U.S. 339, 345-46 (1892).

Equitable cites the PaPUC's approval of its gas cost claim in *Re Gas Cost Rate No. 5* to suggest that its conduct was prudent, in the PaPUC's view, before Act 74 but that it was deemed not prudent on identical facts in the case that resulted in a $14.3 million disallowance under Act 74. However, the facts presented to the PaPUC in these two cases were different and justified different results. During the period under review in *Re Gas Cost Rate No. 5* Equitable had not declared *force majeure* and adopted a policy of paying only for gas actually taken. These new facts justifiably produced a different assessment by the PaPUC of whether Equitable had obtained the lowest cost gas available.

Equitable's investors faced no greater or different regulatory risk after the passage of Act 74. A utility's ability to recover out-of-pocket gas cost expenses prior to Act 74 was dependent upon management making reasonable, prudent, low cost choices when it purchased gas. Act 74 introduced no new or novel requirement that investors could not have anticipated.[7]

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[7] The PaPUC observes that the Court of Appeals never addressed the issue of whether Act 74 introduced a new legal standard to Pennsylvania gas cost recovery proceedings that changed investors' expectations. The Court of Appeals did not have the opportunity to consider this argument because Kentucky West raises it for the first time in its Petition to this Court. The argument raised by Kentucky West before the Court of Appeals regarding retroactivity went to the issue of whether the PaPUC could make *any* disallowance with respect to a prior historic period. Kentucky West never contended before the Court of Appeals that Act 74 introduced new or different legal standards. C.A. App. 827-829. Certiorari should not be granted to address issues not previously raised in the Court of Appeals.

Kentucky West criticizes the Court of Appeals for concluding that Equitable voluntarily accepted the standards of Act 74 for the period July 1983 to July 1984 when it made a filing under the Act rather than pursue its costs under Section 1308 of the Public Utility Code, 66 Pa. C. S. §1308, which governs general rate cases. Petitioners assert that the Court was in error since the "least cost fuel procurement" standard is mandated in Section 1308 cases as well. The PaPUC, however, disputes Petitioner's new contention that it faced a new regulatory standard in claiming gas cost expenses after Act 74 became effective. Therefore the issue of whether a particular type of rate proceeding granted more or less protection from regulatory scrutiny is irrelevant.

In addition to not having established that the PaPUC retroactively applied a new legal standard regarding gas cost recovery, Kentucky West has failed to demonstrate that any "taking" of its property has occurred. Factors relevant to a litigant's substantiation of a public taking include the ecomonic impact of the regulation, the degree to which the action interferes with investment-backed expectations and the character of the governmental action. *Loretto v. Teleprompter Manhattan CATV Corp.*, 458 U.S. 419, 432 (1982), *citing Penn Central Transportation Co. v. New York City*, 438 U.S. 104, 124 (1978). In this case Kentucky West has not proven that the PaPUC's action has prevented Equitable from meeting its operating expenses and moving forward as a business entity. The economic impact of the governmental action does not establish that a taking has occurred. Moreover, the rate adjustment reflected application of long-standing notions of what constitutes a reasonable expense that should be permitted in rates. Investment-backed expectations have therefore not been disrupted by the PaPUC order. Finally, the character of the gov-

ernmental action, disallowance of an unreasonable expense by a state utility commission, weighs heavily in favor of a rejection of the takings argument. Protection of the public from unreasonable rates is part of the long recognized police power of the states. *Arkansas Electric Cooperative Corp. v. Arkansas Public Utility Commission*, 461 U.S. 375 (1983).

Allegations of unconstitutional takings in a ratesetting context have been governed for the past forty years by this Court's holding in *FPC v. Hope Natural Gas Co.*, 320 U.S. 591 (1944). *Hope* has effectively taught for these intervening decades that investor property interests are implicated only if the end result of a rate order causes significant harm to investors. Indicia of significant harm could include insufficient revenue for operating expenses and capital costs such as service on debt and dividends. *Hope* at 603. Even if evidence of such harm is presented, an unconstitutional "taking" has not been established if consideration of consumer interests justifies the rate disallowance. *Id.* In *Hope*, the Court found confiscation nowhere in sight even though the return allowed, under the utility's rate base assumptions, was "meager". *Hope* at 605. Similarly, Equitable's calculation of a "meager" return on equity does not establish that confiscation has occurred. Petitioners have not produced threshold evidence of financial harm of the type that justifies a further judicial inquiry into the issue of whether consumer and investor interests were properly balanced.[8] Kentucky West has made no showing that it is

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[8] Kentucky West's reference to an absence of return on equity does not necessarily constitute a showing of significant harm to investors such that a court must engage in an evaluation of whether ratepayer and shareholder interests have been properly balanced. It is significant that Kentucky West has not substantiated a diminished capacity or an inability to raise capital or meet operating expenses.

the victim of a confiscatory rate order through the retroactive imposition of a new legal standard for ratemaking. The PaPUC's application of Act 74 to Equitable does not present an important issue that requires review by this Court.

This Court's notation of probable jurisdiction in *Duquesne Light Co. v. Barasch, prob. juris noted*, U.S. , 108 S.Ct. 1105 (1988) does not provide grounds for granting review of this case. *Duquesne Light* concerns a utility's effort to recover its investment in cancelled nuclear projects on the grounds that all prudent investment should be recognized in retail rates. The Pennsylvania Supreme Court interpreted Section 1315 of the Public Utility Code, 66 Pa. C. S. §1315, to prohibit the recovery of any costs incurred in the construction of electric utility plants until such property is "used and useful" regardless of the prudence of the investment. The issue of whether prudent investment must be allowed in rates does not arise in the present case because Equitable's expenses have been deemed to fail the test of prudence. Furthermore, there is no evidence that the statutes involved in the present case, Act 74, involve a new legal standard that was given retroactive effect as has been alleged in *Duquesne Light*. Consolidation of this case with *Duquesne Light* is inappropriate given the significant differences of fact and law that exist between these proceedings.

D. The Decision of the Court of Appeals in no Way Conflicts With This Court's Prior Rulings on a Person's Right to Counsel, or Free Speech

Supreme Court Rule 17.1(c) provides that when determining grants of certiorari the Court will consider whether the decision below is in conflict with "applicable decisions of this Court" on federal questions. Kentucky

West has alleged that the decisions below, beginning with that of the PaPUC, have deprived it of its right to counsel and infringed upon its freedom of speech. Petition at 24-28. Although Kentucky West appears to be abandoning its right to counsel arguments in favor of the free speech claim, both positions are nonetheless groundless.

As part of its annual investigation under Act 74, the PaPUC examined whether Equitable had fully and vigorously "represented the interests of its ratepayers before the FERC". App., *infra,* 145a-148a. This is an inquiry mandated by Sections 1317 and 1318 of Act 74. 66 Pa. C. S. §§1317, 1318. App., *infra,* 172a, 174a. The propriety of the PaPUC's directive that Equitable obtain its own counsel in Kentucky West cases is clear if one examines the relationship of these two companies.

Equitable sells gas at the retail level in the Pittsburgh area. It is owned by Equitable Resources, Inc. ("Equitable Resources") which also owns Kentucky West Virginia Gas Company, an interstate gas pipeline. Only Equitable is subject to the jurisdiction of the PaPUC and it alone is subject to the PaPUC's order below. Equitable is a major purchaser of natural gas from its sister company, Kentucky West. These transactions are regulated by the FERC.

The PaPUC found that although Equitable vigorously participated in FERC rate actions involving its other gas pipeline suppliers, it, by its own admission, "does not participate as actively in Kentucky West FERC proceedings as it does in those involving Texas Eastern and Tennessee [its other suppliers]". App., *infra,* 146a. It was Equitable's position before the PaPUC that the participation of other intervenors at FERC justified its failure to participate in the rate cases of its affiliated supplier, Kentucky West. The PaPUC noted that interlocking relationships exist among

Equitable, Equitable Resources and Kentucky West. App., *infra*, 147a.

> Equitable's ratepayers have the right to expect the utility to represent in an effective manner their interests before the FERC in proceedings involving all of Equitable's pipeline suppliers. A serious question arises as to whether such representation can take place in view of Equitable's present corporate structure.

App., *infra*, 148a.

In an attempt to remedy this potential conflict of interests, the PaPUC adopted the recommendation of its Trial Staff that Equitable be directed to obtain counsel and technical support staff "wholly separate from Kentucky West". App., *infra*, 148a. It is in this context that the Equitable Companies complain they have been deprived of the choice of counsel.

The District Court declined to rule on this issue, stating that the PaPUC could bring this matter to the FERC. App., *infra*, 43a. However, the Court of Appeals examined the question and sustained the PaPUC's decision. The Court noted that the right to counsel does not necessarily guarantee the right to choose a particular attorney. App., *infra*, 38a.

> Inherent in the right to counsel is the right to the assistance of counsel unimpaired by the conflict arising from joint representation.
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> * * *
>
> [W]here there exists a potential for conflict, ordering parties to retain separate counsel violates neither due process nor the APA [Administrative Procedure Act].

App., *infra*, 38a; citations omitted. This is the full extent of the PaPUC's order. It has done nothing more than direct Equitable Gas to retain *independent* counsel.

The Equitable Companies posit that "the order requires Equitable to hire counsel to make arguments contrary to the interests of its sister company, Kentucky West." Petition at 27. It states that it is being forced to appear at an administrative proceeding and to hire counsel to advocate positions with which it disagrees. Petition at 25.

With respect to the former statement, the PaPUC has never ordered Equitable to take positions *contrary* to that of Kentucky West. Equitable was directed to defend the interests of its own customers which, at the FERC, coincide with those of Equitable itself. For example, by striving to keep the prices of its pipeline suppliers low, Equitable can keep its supply expenses to a minimum and minimize the gas bills of its customers.

As this Court has noted, the primary purpose of Pennsylvania public utility law is to "serve the interests of the public". *Jackson v. Metropolitan Edison*, 419 U.S. 345, 352 n. 8 (1974). Regulation to such ends is permissible when it comports with due process of law.

> The Fifth Amendment, in the field of Federal activity, and the Fourteenth, as respects state action, do not prohibit governmental regulation for the public welfare. They merely condition the exertion of the admitted power, by securing that the end shall be accomplished by methods consistent with due process. And the guaranty of due process . . . demands only that the law shall not be unreasonable, arbitrary, or capricious, and that the means selected shall have a real and substantial relations to the object sought to be attained.

Nebbia v. New York, 291 U.S. 502, 525 (1934).

The PaPUC's goal, of insuring that Equitable's customers are able to purchase natural gas service at the lowest reasonable cost, is no different than that of virtually every other state public utility commission as well as the FERC.

In order to accomplish that goal the PaPUC has merely directed that Equitable, as a buyer of gas, should retain counsel independent of Kentucky West, the seller of the gas. The Court of Appeals correctly found this remedy to be in conformity with federal law. As such, there is no controversy for this Court to decide.

The reliance by the Petitioners upon *Walters v. National Assn. of Radiation Survivors*, 473 U.S. 305 (1985) is misplaced. The Court, in *Walters*, sustained a federal statute which limited attorneys' fees to $10 for veterans seeking benefits for service-connected death or disability. *Walters, supra*, at 307. Two veterans' organizations and a number of veterans had maintained that the limit on attorney awards effectively prevented veterans from obtaining counsel when appearing before the Veterans Administration's Board of Veterans' Appeals ("BVA"). The government argued that the system was set up to be informal so that veterans could represent themselves alone or with the assistance of veteran groups. The administrative system was non-adversarial in nature with ambiguities always being resolved in favor of the veteran. *Id*. at 310-312. This Court reversed a District Court order which had struck down the $10 limit. The Court held that where there was no adversarial trial-type proceeding, the "need for counsel is considerably diminished". *Id*. at 333-334.

The *Walters* decision is inimical to the First Amendment argument set forth by the Petitioners that Equitable Gas must argue against Kentucky West's interests. In dis-

missing the veterans' claim that a lack of an attorney did violence to a veteran's right to free speech before the BVA, the Court held that so long as the veteran could effectively present his or her case without an attorney there was no bar to free speech. *Id.* at 334-335. In short, an attorney was not necessary to ensure that a veteran's position would be fully presented in the BVA proceedings.

The situation *sub judice* is clearly distinguishable from *Walters*. Equitable has been directed to obtain independent counsel. It is in no way being deprived of counsel.

The Equitable companies will find no solace in their reliance upon *Pacific Gas and Electric Co. v. Public Utilities Comm. of California*, 475 U.S. 1 (1986). As the Court is aware, in *Pacific Gas* it struck down an order of the California PUC which gave a consumer group access to the unused portion of Pacific Gas and Electric Company's (PG&E) monthly customer billing envelopes four times a year. The Court held that this order forced PG&E to use its property, the unused portion of the envelope, to facilitate the expression of views with which it did not agree. *Pacific Gas, supra*, at 12. The Court also found that this forced PG&E to respond to the speech with which it disagreed. *Id.* at 15-17. The Court indicated that had access to the envelopes been content-neutral or had the PUC's order been narrowly tailored to serve a compelling state interest it would have been permissible. *Id.* at 13, 19.

The PaPUC submits that its order is in fact content-neutral and that Equitable has not been forced to take a position adverse to its own interest. The PaPUC's order in no way dictated what Equitable must say or do in FERC proceedings, merely that it operate independently of its affiliate Kentucky West in cases dealing with Kentucky West's rates or services.

In fact, in Equitable's most recent Act 74 proceeding, the PaPUC found, over OCA's objections, that the Company had been vigorously representing its customers' interests before the FERC. *Pennsylvania Public Utility Comm. v. Equitable Gas Co.*, 87 PUR 4th 131, 168 (1987). Although Equitable claims it will be forced to take positions with which it disagrees, experience has shown that this is not the case.

Even if Equitable's allegation were true, the PaPUC submits that its order is narrowly tailored to enforce a legitimate state interest. The PaPUC has merely directed that Equitable represent only its own interest or that of its customers rather than that of its sister company. The PaPUC's order will in no way prevent Kentucky West from advocating its own views before the FERC. Equitable Gas and Kentucky West are purportedly separate operating companies. That each should have separate counsel, in at least some proceedings, is well within the realm of reason and no hardship is created.

Kentucky West points out that parties such as the PaPUC and OCA can also appear at FERC to suggest that the PUC's order requiring separate counsel is unconstitutionally broad given the state interest to be protected. However, this argument essentially goes to the wisdom of the Pennsylvania General Assembly's mandate that *utilities* represent their customer's interests at FERC given that the OCA or PaPUC may also participate in a Kentucky West rate case. Petitioners attempt to add the *voluntary* efforts of OCA and the PaPUC at FERC to the *requirement* that Equitable represent itself in Kentucky West cases so as to make Act 74 an overly broad means of accomplishing a legitimate governmental interest. However, *Act 74* does not compel duplicative representation of ratepayers by OCA and PaPUC in Kentucky West cases.

E. Petitioners' Claims That They Have Been Denied the Right to Counsel and Due Process Rights With Respect to Free Speech Have Been Presented to This Court Prematurely

It is a general principle of law that federal courts will not take appeals where the order complained of has not adversely affected the complainant "but only affects his rights adversely on the contingency of future administrative action". *Hope*, *supra*, at 619; citation omitted. As stated above, although the instant order was issued by the PaPUC some three years ago Equitable Gas has not demonstrated that it has suffered any harm with respect to the PaPUC's direction to hire independent counsel. Until such time as it is able to demonstrate that it has been harmed, this issue is not ripe for review.

CONCLUSION

This Court should deny the Petition for a Writ of Certiorari for the reasons set forth above.

Respectfully submitted,

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CERTIFICATE OF SERVICE

This will certify that completed copies of the Brief of Respondent, Pennsylvania Public Utility Commission in Opposition to the U.S. Supreme Court of the United States were forwarded this date, September 19, 1988 by First Class Mail.